

Message Text

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C O N F I D E N T I A L REYKJAVIK 1104

E.O. 11652: GDS
TAGS: PINT, IC
SUBJECT: COALITION AGREEMENT MAY BE NEAR

REF: REYKJAVIK 1089 DTG 181528Z AUG 78

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SUMMARY: NEGOTIATORS FOR PEOPLE'S ALLIANCE (PA), SOCIAL
DEMOCRATS (SDP), AND PROGRESSIVES (PP) HAVE REACHED AGREEMENT
ON SHORT-TERM MEASURES WHICH PROPOSED LEFT-OF-CENTER GOVERN-
MENT WOULD IMPLEMENT IN ORDER TO DEAL WITH PRESENT ECONOMIC
PROBLEMS. REMAINING MATTERS TO BE DISCUSSED ARE ECONOMIC
PROGRAM FOR LONGER TERM, FOREIGN POLICY, DOMESTIC MATTERS
(NOT DIRECTLY RELATED TO ECONOMICS), AND ALLOCATION OF
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MINISTRIES. LATTER IS SHAPING UP AS MOST CRITICAL ISSUE
STILL TO BE DISCUSSED. END SUMMARY.

1. SHORT-TERM ECONOMIC PROGRAM HAS ALWAYS BEEN REGARDED
AS MOST DIFFICULT POINT DURING ALMOST NINE WEEKS OF TALKS
ON GOVERNMENT FORMATION, THREE PARTIES HAVE NOW REACHED
AGREEMENT ON FOLLOWING PROGRAM: DEVALUATION OF 15 PERCENT;

GENERAL REDUCTION IN PRICES OF 10-12 PERCENT; LOWERING OF INTEREST RATES ON LOANS TO BUSINESS; INCREASE IN PERSONAL INCOME TAX RATES FOR HIGHEST BRACKETS (COUPLES EARNING OVER \$20,000 ANNUALLY); INCREASE IN BUSINESS TAXES; INCREASED TAXES ON CARS, ALCOHOL, AND TOBACCO; REDUCTION IN GOVERNMENT SPENDING. EMBASSY UNDERSTANDS THAT PARTIES HAVE ALSO REACHED INFORMAL AGREEMENT AMONG THEMSELVES AND WITH LEADERS OF LABOR TO ELIMINATE ALL RESTRICTIONS ON COST-OF-LIVING WAGE HIKES WHICH ARE CALCULATED AS PERCENTAGE OF BASIC WAGE. IN RETURN, LABOR WOULD NOT SEEK INCREASE IN BASIC WAGES WHEN CONTRACT EXPIRES DECEMBER 1.

2. SOCIAL DEMOCRATS BELIEVE OTHER PARTS OF GOVERNMENT PROGRAM MAY NOW FALL INTO PLACE WITH RELATIVE EASE. PRELIMINARY DISCUSSIONS BETWEEN SDP AND PA HAVE REPORTEDLY INDICATED PA WILLINGNESS TO WRAP UP OUTSTANDING MATTERS QUICKLY AND LARGELY ON SDP TERMS, WITH DIFFERENCES OVER DOMESTIC AFFAIRS IRONED OUT IN ONE OR TWO SESSIONS. AS FOR FOREIGN POLICY, PA CHAIRMAN LUDVIK JOSEPPSSON HAS ALREADY STATED THAT HIS PARTY CAN SET ASIDE ITS OPPOSITION TO CONTINUED PRESENCE OF NATO BASE IN ORDER TO ALLOW NEW GOVERNMENT TO DEAL WITH ECONOMIC MATTERS (REFTEL). PROGRESSIVES HAVE NOT POSED ANY PROBLEM IN NEGOTIATIONS SO FAR; THEY ARE NOW SO ANXIOUS TO BE PART OF NEXT GOVERNMENT THAT THEY HAVE READILY ACCEPTED WHAT-EVER HAS BEEN DECIDED BILATERALLY BETWEEN PA AND SDP.

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3. ONLY SERIOUS HURDLE REMAINING TO GOVERNMENT FORMATION APPEARS TO BE DISTRIBUTION OF CABINET SEATS AND THIS MAY YET CAUSE BREAKDOWN IN CURRENT NEGOTIATIONS. SINCE PA HOLDS MANDATE TO BUILD COALITION, PARTY WANTS, AND WOULD NORMALLY BE ENTITLED TO, PRIME MINISTRY FOR ITSELF. SDP FIRMLY RESISTING THIS ARGUING THAT ICELAND'S PRO-NATO POLICY WOULD BE JEOPARDIZED WITH PA IN EITHER PRIME MINISTRY OR FOREIGN MINISTRY. SOCIAL DEMOCRATS WILLING TO YIELD ON ANY PORTFOLIOS OTHER THAN THESE TWO, AND SOURCES WITHIN PARTY HAVE PRIVATELY STATED THAT IT WOULD BE PREFERABLE TO END THE THREE-PARTY TALKS RATHER THAN GIVE IN TO PA ON THIS POINT. PROGRESSIVES' TWO NEGOTIATORS MUN TALKS ARE

SPLIT ON MATTER WITH PP CHAIRMAN OLAFUR JOHANNESSEN FAVORING PA FOR PRIME MINISTRY WHILE STEINGRIMUR HERMANNSSON (A PROSPECTIVE MINISTER OF INDUSTRY) SUPPORTING SDP. ALTHOUGH PARTICIPANTS IN TALKS BELIEVE THAT FINAL AGREEMENT CLEARING WAY FOR LEFT-OF-CENTER COALITION MAY BE NEAR, IT IS QUITE POSSIBLE THAT PROBLEM OF CABINET MINISTRIES COULD WRECK DISCUSSIONS.
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